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071613Z Jan 05

UNCLAS SECTION 01 OF 02 ANKARA 000110

SIPDIS

TREASURY FOR INTERNATIONAL AFFAIRS - RADKINS AND MMILLS
NSC FOR BRYZA AND MCKIBBEN

SENSITIVE

E.O. 12958: N/A
TAGS: EFIN TU
SUBJECT: Turkey: New Bond Issue Signals Increasing Confidence

¶1. (SBU) Summary: Amid signs of increased foreign investor interest in Turkish lira assets, especially longer maturities, the World Bank has issued a 5-year Turkish Lira bond. Turkish financial officials are not concerned the new instrument would compete with Government paper. The World Bank issuance helps to develop Turkish financial markets and pave the way for longer-dated Turkish government issues which reduce dependence on rolling over short-term debt -- a key remaining element of Turkey's continuing vulnerability to sudden shifts in market confidence. End Summary.

¶2. (U) The IBRD (World Bank) issued a 5-year Aaa/AAA rating Turkish Lira annuity note of 70,000,000 new Turkish Lira ($50.7 million) through Citibank on December 23, with January 7, 2005 settlement date and 15% coupon yield. The issuance is significant in several respects: it takes the lira yield curve out 2 years further than the 3-year bond which Turkish Treasury only introduced in October; it is a rare lira issuance by an investment-grade borrower not based in Turkey; and it yields a substantially lower rate that any existing lira paper.

¶3. (SBU) The issuance of the World Bank notes is probably related to signs of increased appetite for Turkish assets by foreign investors. With positive prospects from a new IMF agreement, a date to begin accession negotiations from the EU and continuing positive macroeconomic performance, Central Bank Markets department Director-General Cigdem Kose told econ specialist that Turkish markets were attracting a broader base of prospective portfolio investors. Following Treasury's successful $500 million Eurobond issuance in November, Kose said that IBRD -- and even JP Morgan -- were interested in issuing Turkish Lira instruments for foreign investors. She said that the IBRD Turkish Lira note issuance on December 23 signaled a new customer profile for Turkish markets, i.e. investors that would like to enjoy high Turkish Lira yields without taking country risk. For example, Kose said a Canadian investment company named TD Securities visited the Central bank recently and said it would be introducing new customers to Turkish markets.

¶4. (SBU) Volkan Taskin, DG for domestic debt at the Turkish Treasury told econ specialist that the Treasury welcomes such developments since they share the view that Turkish Lira note issuance can help them to extend the yield curve for lira debt instruments. Taskin said at this stage Turkish Treasury was not capable of reaching out to all customers like those who would like to invest in Turkish Lira instrument without any country risk, or those whose investment criteria is limited to certain level of rating. Taskin said the IBRD issuance would also help deepen the market in lira instruments and he has heard that there could be other similar issuances soon.

¶5. (SBU) Kose's Deputy, Emrah Eksi, also said that after December 17, the CBT tracked about a capital inflow of about $1 billion into Turkey and since May 2004, the CBT noted a $500 million and $1 billion increase in USD and Euro accounts in banking system.

¶6. (SBU) World Bank Financial Economist Rodrigo Chavez confirmed that the issuance was done in cooperation with the Turkish Treasury under an umbrella agreement in place since 2002. The issuance is part of a program by the World Bank to issue notes in "non-core" (i.e. emerging market) currencies. Chavez said the buyers of this paper are small banks in Western Europe who are interested in Turkish lira yields but are constrained by regulatory requirements from buying lower-rated Turkish country risk.

¶7. (SBU) Comment: The World Bank issuance is modest in size, and has no direct impact on the government's debt situation. On the other hand, coming at a time of

increased investor interest in Turkey, it demonstrates that even conservative investors are interested in Turkish Lira assets, if not Turkish country risk. By going out five years (i.e. extending the yield curve), it may help pave the way for longer-dated issues by the GOT which help reduce the government's dependence on rolling over its mostly short-term domestic debt, which is the major factor in Turkey's continuing financial vulnerability to financial crises resulting from short-term swings in markets.

Edelman